



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

April 12, 2000



MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

for Charles O. Rossotti *Prokhorov*
Commissioner of Internal Revenue

SUBJECT:

Draft Audit Report - The Internal Revenue Service Needs to
Improve Its Coordinated Oversight of the Substitute for Return
Process -- Urmem 2/10/00

Thank you for the opportunity to respond to your draft report entitled "The Internal Revenue Service (IRS) Needs to Improve Its Coordinated Oversight of the Substitute for Return (SFR) Process." The objective of the review was to determine if the IRS could measure the effectiveness of its strategy to bring nonfiling taxpayers into compliance by assessing income tax through the SFR process.

In your report, you recognized that our recently established National Nonfiler Strategy and the Nonfiler Executive Steering Committee provide a good start to improve the SFR process. We agree with your assessment and plan to use the nonfiler strategy, along with your recommendations, to improve SFR policies and procedures. We believe that through these actions we will ensure the equitable treatment of all taxpayers.

Our comments on the specific recommendations in this report are as follows:

IDENTITY OF RECOMMENDATION #1

The Chief Operations Officer should establish uniform policies and procedures to ensure coordination of IRS efforts between the divisions processing SFR accounts.

ASSESSMENT OF CAUSE(S)

The SFR process is performed by three functions in the IRS - Assistant Commissioner (Customer Service), Assistant Commissioner (Examination), and Assistant Commissioner (Collection). Each function has its own fiscal year goals and funding. In the past, the three functions did not have an integrated strategy to address the use of SFR.

CORRECTIVE ACTIONS

A nonfiler strategy has been adopted and is now being implemented. The National Nonfiler Executive will ensure coordination takes place between business operating units and SFR is administered consistently and equitably in Customer Service, Collection, and Examination functions.

IMPLEMENTATION DATE

Proposed – October 1, 2001

RESPONSIBLE OFFICIAL

Assistant Commissioner (Collection)

CORRECTIVE ACTION (S) MONITORING PLAN

The National Nonfiler Executive will track and report to the Chief Operations Officer on the status of the nonfiler strategy.

IDENTITY OF RECOMMENDATION #2

The Chief Operations Officer should coordinate the development of a process to monitor the future filing compliance of taxpayers with SFR tax assessment regardless of which function processed the account. In addition, the costs of processing and resolving SFR tax assessments should be tracked and measured by IRS management.

ASSESSMENT OF CAUSE(S)

The information needed to manage the SFR process is not readily available. Only parts of the cost of resolving a SFR case are available; for example, the IRS can track the costs incurred in service centers and in the Examination function but cannot do this for tax examiners in our Automated Collection System (ACS) or for revenue officers.

CORRECTIVE ACTIONS

The IRS will request programming changes to develop a report that tracks the future compliance of taxpayers that are subject to SFR. Additionally, the IRS will use Research Division to conduct a post-profiling analysis on taxpayers that were subject to SFR treatment for tax year 1996.

Regarding cost benefit of the SFR process, the IRS will use data from the Enforcement Revenue Information System (ERIS) to analyze the SFR cost benefits in the Examination and Customer Service functions annually. This will involve tabulation of labor costs for the ASFR process and the SFR done by Examination employees only. Direct hours for SFR will be derived from ERIS, Examination, and Customer Service reports. It will not include time data for revenue officers or tax examiners in ACS.

The benefit of making an SFR assessment can be judged on the SFR's ability to encourage compliance for the year in question and in the future. Therefore, a historical cost benefit model should not be the paramount issue. We use this enforcement process to bring taxpayers into compliance. Since taxpayers often appeal these assessments and file corrected returns, the process will always have relatively higher labor costs. Since the process relies on third party Information Returns Processing data, and cannot fully determine deductions from income, the process may not determine the taxpayer's liability with exact precision.

The IRS will use data from ERIS, Information Systems, and Research to access the tax administration benefit derived from the SFR process. This process will occur annually to help budget for SFR activity.

IMPLEMENTATION DATE

Proposed - October 1, 2002

RESPONSIBLE OFFICIAL

Assistant Commissioner (Collection)

CORRECTIVE ACTION(S) MONITORING PLAN

The National Nonfiler Executive will coordinate the corrective actions and provide regular status updates to the Chief Operations Officer.

IDENTITY OF RECOMMENDATION #3

The Chief Operations Officer should coordinate the design of a process to profile SFR tax assessments and their resolution regardless of processing function. The IRS should know:

- The amount of total SFR tax assessments.
- The amount of revenue collected on SFR tax assessments.
- The amount of SFR tax assessments eventually abated.
- The amount of SFR tax assessments determined to be uncollectible.

ASSESSMENT OF CAUSE(S)

The traditional approach to inventory management does not track whether SFR tax assessments were eventually resolved as abatements or as currently noncollectible.

CORRECTIVE ACTIONS

We will secure ERIS data on an annual basis that reflect this information. We will analyze this information for significant trends and the identification of followup issues. The staff of the National Nonfiler Executive will coordinate the analysis.

IMPLEMENTATION DATE
Proposed – January 1, 2001

RESPONSIBLE OFFICIAL
Assistant Commissioner (Collection)

CORRECTIVE ACTION (S) MONITORING PLAN
The National Director, Collection Redesign, will monitor this corrective action and provide regular status reports to the Chief Operations Officer.

If you have any questions or need additional information, please call me, or a member of my staff may contact Charles W. Peterson, Assistant Commissioner (Collection), at (202) 622-5100.